MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 3, 2016/2017

BFE2074 – FINANCIAL ECONOMICS
(All Sections / Groups)

02 JUNE 2017
9:00 a.m – 11:00 a.m.
(2 Hours)

INSTRUCTIONS TO STUDENTS

1. This question paper consists of **THREE (3)** pages with **FIVE (5)** questions only.

2. Attempt **ALL** questions. The distribution of the marks for each question is given.

3. Please write all your answers in the Answer Booklet provided.

ANSWER ALL QUESTIONS (100 Marks)

Question 1

(a)   Define the term international economic integration.

(3 marks)

(b)   Explain the difference between portfolio investment and foreign direct investment by giving an example each.

(4 marks)

(c)   **Table 1**

	Goods	Services	Income	Unilateral Transfers	Current Account
Debit					
Credit					

Reproduce Table 1 in your answer booklet and show the debit and credit entries in each balance of payments account for the following transactions:

(i)   The government gives financial aid (BRIM) of RM1,200 to each family with household income below RM3,000.

(2 marks)

(ii)   A local company imports a RM10,000 winter jackets.

(2 marks)

(d)   What is the relationship between a nation's current account balance and its capital flows?

(2 marks)

(e)   Discuss what will happen to current account balance if a nation is experiencing:
(i)   Net capital inflows
(ii)   Net capital outflows

(2 marks)
(Total: 15 marks)

Question 2

(a)   Given the U.S dollar per euro as 1.0989 $/€, and the U.S. dollar per Canada dollar 0.7246 $/C$, calculate:
(i)   The Canadian dollar price of the euro (C$/€)

(2 marks)

Continued...

(ii)   The Euro price of the U.S. dollar (€/$)

(2 marks)

(Please take four decimal points for all your calculation)

(b)   Suppose we observe the following information for Mexico, China and Malaysia. The exchange rates given in Table 2 are the currency-per-Malaysian ringgit rates. The bilateral weight assigned to Mexico is 0.4 and China is 0.6.

Table 2

	S(2010)	S(2014)	CPI(2010)	CPI (2014)
Mexican Peso	3.05	3.00	116.5	125.2
Chinese Yuan	2.32	2.57	86.5	100.25
Malaysia			99.5	110.2

Note: S is the spot exchange rates and CPI is the consumer price index

(i)   Using the information in Table 2, calculate 2010 and 2014 real effective exchange rates of the Malaysian ringgit (Please take two decimal points for all your calculation).

(10 marks)

(ii)   Do the values you calculated indicate an appreciation or depreciation of the Malaysian ringgit?

(2 marks)

(iii)   Based on part (ii), calculate the rate of appreciation or depreciation.

(1 mark)

(c)   What is Purchasing Power Parity (PPP)?

(3 marks)
(Total: 20 marks)

Question 3

(a)   What is forward exchange rate? Suppose the spot rate is 1.3222 $/£ and the one month forward rate is 1.3624 $/£. Is the pound currency is trade at a forward discount or forward premium? Is the dollar currency is trade at a forward discount or forward premium? Calculate the forward discount or forward premium on the pound currency (Please take two decimal points).

(8 marks)

(b)   Construct diagrams representing (1) the spot exchange rate market for pound relative to the U.S. dollar, (2) the forward exchange rate market for pound relative to the U.S. dollar, and (3) the loanable funds market in the United States as individuals move funds from dollar-denominated instruments to pound-denominated instruments.

(9 marks)
Continued...

(c)   Based on part (b), what will happen to the value of pound currency and United
        States interest rate?
                                                                                    (3 marks)
                                                                            (Total: 20 marks)

Question 4

(a)   Illustrate a simplified balance sheet of the central bank.
                                                                                    (4 marks)

(b)   What is the monetary approach to balance-of-payments and exchange-rate
        determination? Do you agree that under a fixed-exchange-rate arrangement, the
        monetary approach indicates that an increase in domestic credit generates a
        balance-of-payments deficit? Explain.
                                                                                    (11 marks)
                                                                            (Total: 15 marks)

Question 5

(a)   Define the IS schedule and list the factors that shift the IS schedule rightward.
                                                                                    (5 marks)

(b)   Define the LM schedule and list the factors that shift the LM schedule rightward.
                                                                                    (5 marks)

(c)   Define the balance-of-payments (BP) schedule.
                                                                                    (4 marks)

(d)   Graphically explain how the initial effects of expansionary monetary policy action
        with fixed exchange rate and high degree of capital mobility affects the balance-
        of-payments, nominal interest rate and real income. What is the key contribution
        to the resulting of your balance-of-payments?
                                                                                    (16 marks)
                                                                            (Total: 30 marks)

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